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No. 90-647

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

C.L. GRIMES,

Petitioner,

v.

CENTERIOR ENERGY CORPORATION,

Respondent.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF IN OPPOSITION OF RESPONDENT CENTERIOR ENERGY CORPORATION

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QUESTION PRESENTED

Did the Court of Appeals, pursuant to the Securities and Exchange Commission exemption for proposals "relating to the conduct of the ordinary business operations," properly hold that Centerior could exclude from its proxy materials a shareholder proposal limiting capital expenditures, regardless of size, to the amount of dividends distributed in the prior year?

RULE 29.1 STATEMENT

Respondent Centerior Energy Corporation is a publicly held corporation which has neither a parent corporation nor any subsidiary which is not wholly-owned.

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BRIEF IN OPPOSITION OF RESPONDENT CENTERIOR ENERGY CORPORATION

STATEMENT OF THE CASE

Respondent Centerior Energy Corporation ("Centerior") is an Ohio electric utility holding company. Centerior is a publicly held company whose 140 million shares of common stock outstanding are traded on the New York Stock Exchange. As of the date of the filing of the complaint in this action, Petitioner C.L. Grimes ("Grimes") owned less than one percent of the outstanding shares.

Centerior's Articles of Incorporation specifically vest authority to make capital expenditures in the Board of Directors. Grimes informed Centerior's Chairman that he wished to include in the corporation's proxy materials an amendment to the Articles providing that:

> The corporation . . . shall not expend in any calendar year *any* monies by way of capital or construction expenditures in excess of the cash amount paid to the common shareholders as dividends in the preceeding [sic] calendar year, without the formal prior consent of the common shareholders *in each instance.* (Emphasis added).

While the Securities and Exchange Commission ("SEC") shareholder proposal rules require a corporation to include most shareholder proposals in its proxy materials, SEC Rule 14a-8(c), 17 C.F.R. § 240.14a-8(c) sets forth 13 exemptions permitting omission of proposals. Centerior excluded Grimes's proposal because it met the criteria of three of the exemptions: 14a-8(c)(2), 17 C.F.R. § 240.14a-8(c)(2), excluding proposals requiring a company to violate state law; 14a-8(c)(7), 17 C.F.R. § 240.14a-8(c)(7), excluding proposals concerning the conduct of a corporation's ordinary business operations; and 14a-8(c)(13), 17 C.F.R. § 240.14a-8(c)(13), excluding proposals relating to specific amounts of cash or stock dividends.

The SEC's Division of Corporate Finance issued a "no-action" letter concluding that Grimes's proposal was properly excluded by Centerior. Complaint Exhibit 6. The SEC found that Grimes's proposal fell

under exemption 2, permitting Centerior to omit proposals which would cause the corporation to violate state law. Grimes's proposal forces Centerior to violate Ohio laws requiring the company to make expenditures to provide necessary and adequate public service and to pay dividends solely out of surplus. In light of this decision, the SEC did not consider the alternative grounds for exclusion advanced by Centerior. Grimes sought review by the entire Commission, but the SEC declined to overturn the Division's decision.

Grimes next filed suit in the District Court for the District of Columbia seeking an injunction barring Centerior's distribution of proxy materials which did not contain his proposal. Although the District Court noted that Grimes's proposal might require Centerior to violate Ohio law, the court held that Grimes's proposal was omissible under the two other exemptions Centerior raised. Pet. App. 17a-20a. The court held that Centerior correctly omitted the proposal because it related both to the conduct of Centerior's ordinary business (exemption 7) and to specific amounts of cash or stock dividends (exemption 13).

The Court of Appeals for the District of Columbia Circuit affirmed in a unanimous decision. Pet. App. 1a. The Court of Appeals held that Grimes's proposal, by potentially coercing Centerior into seeking stockholder approval of even the smallest capital expenditures, related to Centerior's ordinary business operations and would interfere with management's ability to make the very day-to-day decisions which the shareholders entrust to them. Pet. App. 5a-8a. Having sustained the applicability of exemption 7, the

court did not reach the alternative grounds for omission of Grimes's proposal.

REASONS FOR DENYING THE WRIT

INTRODUCTION

There is no reason for this Court to grant Grimes's petition for a writ of certiorari. Neither of the questions presented is sufficiently important to warrant Supreme Court review. Although he contends that this is a case involving important issues of "shareholder democracy," in truth this suit concerns the routine application of the SEC shareholder proposal rules. Grimes's argument is nothing more than a semantic exercise which has been universally rejected. Furthermore, the Court of Appeals correctly decided the case below based on ample precedent. This is not a case involving an unresolved area of law. The Court of Appeals reached a decision consistent with the SEC's determination that corporations may exclude proposals intruding upon management's ability to make routine capital expenditures.

Finally, this Court should not grant the writ because Grimes's proposal has been held properly excluded under not one but *three* different exemptions to the shareholder proposal rules.

ARGUMENT

1. The Writ Should Be Denied Because There Is No Important Question Presented Before The Court

Grimes frames his case as involving "[t]wo matters of fundamental importance - stockholder democracy and corporate governance." Pet. 1. However, this case merely involves the routine interpretation of an agen-

cy's rules and their application to a narrowly defined set of facts that is consistent with a long line of administrative decisions and the only case law on point. While corporate governance may be an important and "lively" issue, Grimes is seriously mistaken in his belief that *this* is the case which presents that issue for review.[1]

Grimes contends that his proposal relates to the allocation of power, i.e., corporate governance, because it seeks to transfer authority to make certain capital expenditures from the Board of Directors to the shareholders. Pet. 8-10. Following Grimes's argument, every proposal transferring a decision from management to the shareholders is important and thus eligible for Supreme Court consideration. However, the allocation of power is truly significant only if the power transferred is significant. While it would certainly be revolutionary to require shareholder approval of mundane capital expenditures in a large publicly held corporation as encompassed by Grimes's proposal, it is not a matter requiring Supreme Court review.

Grimes seemingly also urges that the Court grant the writ to consider whether proxy materials which fail to mention a properly excluded shareholder proposal are misleading. Footnotes 8 and 9 of the petition

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[1] Grimes, in a particularly frail argument, also urges this Court to grant certiorari because the Supreme Court has never previously considered the shareholder proposal rules and he believes it is unlikely that other shareholders will appeal the denial of the inclusion of their proposals in proxy materials to the Supreme Court level. That the Court has not yet considered an issue or that litigants face a long road to reach the Supreme Court are obvious facts but not appropriate grounds for granting certiorari.

address this issue which even Grimes admits is "not of the same magnitude as . . . the primary issue" but which he argues is of "great practical significance in the administration of the stockholder proposal rules." Pet. 11. However, that resolution of an issue is of "practical significance" to the administration of an agency's regulations is not a proper ground for granting certiorari. Not only is this not an issue of sufficient weight to warrant Supreme Court review, but how the SEC implements its own rules is an area in which the court should defer to the expertise of the agency. *Ford Motor Credit Co. v. Milhollin*, 444 U.S. 555, 566 (1980).

2. The Writ Should Be Denied Because the Court Below Correctly Decided the Issues Presented

This Court should not grant the writ of certiorari because the Court of Appeals fully considered and correctly decided the issues before it. Based on ample SEC precedent, the Court of Appeals properly determined that Centerior could omit Grimes's proposal because it related to Centerior's ordinary business operations. Similarly, the Court of Appeals held that Centerior need not include notice in its proxy materials of an omissible proposal in light of the purpose for which the SEC adopted the shareholder proposal rules and because Grimes's position was totally unsupported by law.

The Court of Appeals followed well established precedent that shareholder proposals concerning a company's capital expenditures are properly excluded under the ordinary business operations exemption. For example, in *General Public Utilities Corp.*, SEC No-Action Letter (Feb. 21, 1980) (Lexis, Fedsec library, Noact file), the SEC found that a shareholder pro-

posal requiring a public utility to incur "capital expenditures for new generating capacity [only in] emergency situations" was properly excluded because it involved "matters relating to the conduct of the ordinary business operations of the issuer (i.e., the levels of service and construction programs of the company)." *See also Florida Power & Light Co.*, SEC No-Action Letter (Jan. 18, 1983) (Lexis, Fedsec library, Noact file) (proposal that Board of Directors "minimize . . . dilution of the equity and earnings of the shareholders" excluded because the "determination of whether or not to . . . reduce capital expenditures" related to company's ordinary business operations); *Allis-Chalmers*, SEC No-Action Letter (March 3, 1982) (Lexis, Fedsec library, Noact file) (proposal restricting company's investment to existing facilities involved conduct of ordinary business operations). The SEC allows such proposals to be excluded because they dramatically interfere with management's ability to operate the company efficiently by using their expertise to make qualified business decisions which are beyond the experience of shareholders. *Western Capital Inv. Corp.*, SEC No-Action Letter (March 16, 1989) (Lexis, Fedsec library, Noact file) (quoting SEC Release No. 34-12999 (Nov. 22, 1976)).

The Court recognized that capital investments requiring very large sums might not relate to ordinary business operations, even in an industry as capital intensive as that of a public utility. However, Grimes's proposal covers *all* capital expenditures, great and small. As the Court observed, "Grimes's proposal would involve them [shareholders] in such minor or routine day-to-day decisions as the purchase of type-

writers or the replacement of worn-out machinery." Pet. App. 8a. These matters indisputably relate to ordinary business however defined.

The Court of Appeals also correctly decided that Centerior's failure to notify shareholders that Grimes would present a proposal at the shareholders meeting which the corporation had rightly excluded from its proxy materials is both consistent with the SEC's goal in regulating shareholder proposals and completely logical. The only authority Grimes could muster in support of his argument below, *New York City Employees' Retirement System v. American Brands, Inc.*, 634 F. Supp. 1382 (S.D.N.Y. 1986) was inapposite.[2] In contrast to the instant suit, *American Brands* concerned a proposal which was *not* excludable under any of SEC Rule 14a-8(c)'s exemptions. Without any precedent to support Grimes's argument, the court turned to the purposes underlying the shareholder proposal rules. The court concluded that "if a proposal falls outside the range of 'proper subjects,' [for shareholder action] as implicitly defined by Rule 14a-8(c), neither the proposal itself nor the fact that its sponsor intends to present the proposal at the next shareholders' meeting need be included in the proxy materials." Pet. App. 9a. Otherwise, no proposal could ever be excluded and the shareholder proposal rules would serve no purpose.

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[2] Curiously, since the Court of Appeals opinion stating that Grimes miscited the *American Brands* holding, Pet. App. 8a, he has not offered any authority in support of his claim that Centerior violated SEC Rule 14a-9(a), 17 C.F.R. § 240.14a-9(a).

3. The Writ Should Be Denied Because There Are Alternative Grounds on Which the Judgment Could Be Affirmed

Even if this Court were to determine that the Court of Appeals wrongly decided that Grimes's proposal fell within the exemption for conduct relating to ordinary business operations, the Court should be aware that at various stages of this litigation, Centerior's omission of Grimes's proposal was upheld under two independent exemptions. Although the Court of Appeals did not reach those issues, either ground would be sufficient to sustain the judgment in this case.

The SEC found that Grimes's proposal was excludable under exemption 2 which permits omission of proposals which "if implemented, would require the [corporation] to violate any state law." The SEC reasoned that adoption of Grimes's proposal would require Centerior to violate two provisions of Ohio law if the shareholders failed to authorize essential capital expenditures. Centerior is under a duty to provide "necessary and adequate service and facilities" to its customers, Ohio Rev. Code Ann. § 4905.22 (Baldwin 1990); an obligation which requires Centerior to incur expenses to meet the present and future demand for electricity. However, if the shareholders did not approve capital expenditures in excess of the amount of dividends distributed during the preceding year, Centerior would not be able to fulfill its statutory obligation to provide "necessary and adequate" service.

Centerior is also constrained by state law to distribute dividends solely from surplus. Ohio Rev. Code Ann. § 1701.33 (Baldwin 1990). The SEC found that

Grimes's proposal might force Centerior to violate this provision because if Centerior sought to avoid a potential shareholder veto of needed capital expenditures in the following year, it would have to declare unusually large dividends. However, if these dividends could not be distributed solely from surplus, Centerior would violate § 1701.33 of the Ohio Code.

In addition, the District Court approved Centerior's reliance upon exemption 13, which permits exclusion of shareholder proposals relating to "specific amounts of cash or stock dividends." The District Court held that Grimes's proposal refers to specific amounts of cash because it potentially creates a formula for the payment of dividends. Pet. App. 20a. To ensure that Centerior could make all necessary capital expenditures, the company would be forced to distribute to the shareholders dividends which were at least equal to the sum of expenditures Centerior anticipated incurring in the upcoming year. This decision is consistent with SEC decisions excluding similar proposals establishing a formula for the payment of dividends. *See, e.g., The Boeing Co.*, SEC No-Action Letter (Jan. 19, 1989) (Lexis, Fedsec library, Noact file) (proposal that company declare a 2 for 1 stock split created a formula); *Citicorp*, SEC No-Action Letter (Feb. 22, 1988) (Lexis, Fedsec library, Noact file) (proposal to increase dividends yearly by at least 10%).

CONCLUSION

For the reasons stated above, the writ of certiorari should be denied.

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